Michigan Economic and Revenue Outlook

FY 2003-04 and FY 2004-05

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December 3, 2004

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December 3, 2004

Revenue Review and Outlook

- FY 2004 GF-GP revenue is projected to increase 0.1 percent to $7,968.1 million, a $2.3 million reduction from the adjusted May Consensus estimate. SAF revenue is expected to fall 1.5 percent to $10,551.9 million, $7.4 million below the adjusted May Consensus estimate.
- FY 2005 GF-GP revenue is projected to decline 0.9 percent to $7,899.0 million. This total is $196.4 million below the adjusted May Consensus estimate. SAF revenue is projected to increase 3.7 percent to $10,944.0 million, $52.7 million below the adjusted May Consensus estimate.

2004 and 2005 U.S. Economic Outlook

- Real Gross Domestic Product growth is forecast to average 4.4 percent in 2004 and 3.3 percent in 2005.
- After cooling over the summer, national payroll employment strongly increased in October (337,000 jobs). Wage and salary employment has grown each month for over a year and is erasing the job losses since the beginning of the last recession. However, payroll employment is still about half a million jobs below the March 2001 peak. Employment is projected to continue growing over the forecast horizon. The U.S. unemployment rate is forecast to average 5.5 percent and 5.4 percent in 2004 and 2005, respectively.
- Historically low interest rates have provided consumers with the ability to purchase housing at record levels and refinance existing mortgages. However, with wage and commodity price pressures building, interest rates are projected to increase throughout the forecast period.
- Low capacity utilization rates will constrain investment, but the need to replace increasingly obsolete machinery, tax incentives that expire in 2004 for new investment in equipment, and higher profits will help spur investment.
- Light vehicle sales are forecast to be 16.7 million units in both 2004 and 2005, relatively stable from the past two years.
- Consumer price inflation is forecast to be moderate, averaging 2.7 percent in both 2004 and 2005.

2004 and 2005 Michigan Economic Outlook

- Michigan wage and salary employment is forecast to grow modestly throughout the forecast period. However, Michigan wage and salary employment is expected to register its fourth straight year of decline (-1.1 percent) in 2004. In 2005, Michigan wage and salary employment is forecast to grow 0.5 percent.
- The Michigan unemployment rate is forecast to fall to 6.7 percent for 2004. In 2005, the Michigan unemployment rate is forecast to rise to 6.9 percent.
- Wage and salary income will post a modest gain (2.4 percent) in 2004, and increase at a faster pace of 4.3 percent in 2005. Personal income will post moderate increases throughout the forecast horizon. In 2004 and 2005, personal income is forecast to rise 3.8 percent and 5.4 percent, respectively.
- In FY 2004 and FY 2005, Michigan wage and salary income is expected to grow 2.5 percent and 3.5 percent. Disposable income is expected to rise 4.6 percent and 4.4 percent in FY 2004 and FY 2005.

Forecast Risks

- Nationally, employment has increased each month for over a year. However, Michigan job growth has remained elusive. The forecast projects moderate gains in Michigan employment. If businesses lose confidence in the expansion, both national and Michigan employment growth may be slower than forecast.
- Business investment is key to the continued economic expansion. If firms invest more than expected, growth may be stronger than forecast.
- Michigan manufacturing employment has declined sharply over the past few years. In 2004, Michigan manufacturing employment is forecast to decline at slightly a slower rate than in 2003. Similarly, manufacturing declines are forecast to slow still further in 2005. If Big Three market share falls precipitously, manufacturing employment could decline more steeply.
- Continued higher oil and natural gas prices could curb growth. Weaker growth abroad could also slow domestic growth by reduced exports.
- A rapidly falling dollar, while helping the manufacturing sector and exports, could also spur inflation and lead to instability for U.S. financial markets. Slower equity price growth or outright declines could slow consumption and investment spending.
- If firms add to their inventories faster (slower) than projected, economic growth will be more (less) rapid than projected.
- Geopolitical concerns continue to pose a risk to the forecast.

ECONOMIC REVIEW AND OUTLOOK
December 3, 2004

Current U.S. Economic Situation

Summary

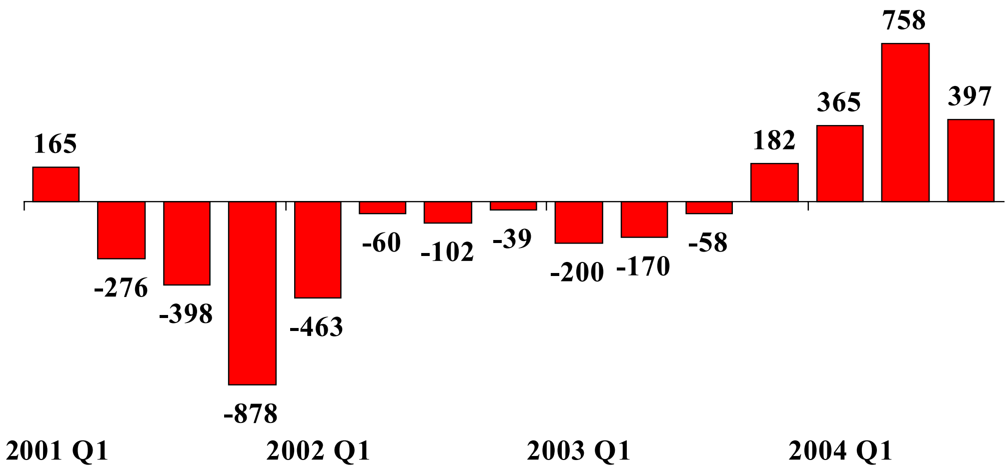
The current recovery is now three years old, having begun in November 2001. Over the past six quarters, real GDP growth has exceeded 3.0 percent each quarter. With the exception of the second quarter this year, consumption growth has been strong over this period. Similarly, with the exception of the first quarter of this year, equipment and software investment has grown at double digit rates over the past year and a half, spurred by higher profits and tax incentives that expire at the end of 2004. Light vehicle sales have remained strong throughout the recovery, boosted by record incentives and low financing rates. Supported by historically low interest rates, new and existing home sales have remained strong as well.

However, employment growth has lagged the recovery. Employment declined each quarter during the recovery until the fourth quarter of 2003. While employment has grown in each of the past four quarters, that growth has been uneven. Employment reported tepid growth the last quarter of 2003 and moderate growth in the first quarter of 2004; employment then surged in the second quarter of this year before moderating in the third quarter. Employment recorded strong growth in October. Further, despite recent growth, U.S. payroll employment remains a half million jobs below its March 2001 peak. Continued job growth will be key to sustained economic growth.

Interest rates have remained at historically low levels, but are expected to rise as the economy continues to report solid growth and inflationary pressures build with higher commodity prices and wage pressures as job growth increases. Energy prices, most notably oil, are increasing due to a restricted supply and growing world demand. In recent weeks, oil prices have hovered around $50 a barrel. Security concerns for oil supplies are also in the forefront with tensions high in Iraq and the Middle East and other oil producing nations.

Federal government spending is expected to remain solid in the near-term with defense spending remaining robust through the middle of 2005. Federal government spending is then expected to slow as defense expenditure growth decelerates. State and local government spending is expected to remain weak through most of the forecast horizon.

US Payroll Employment Growing
(Quarterly Change in Thousands)

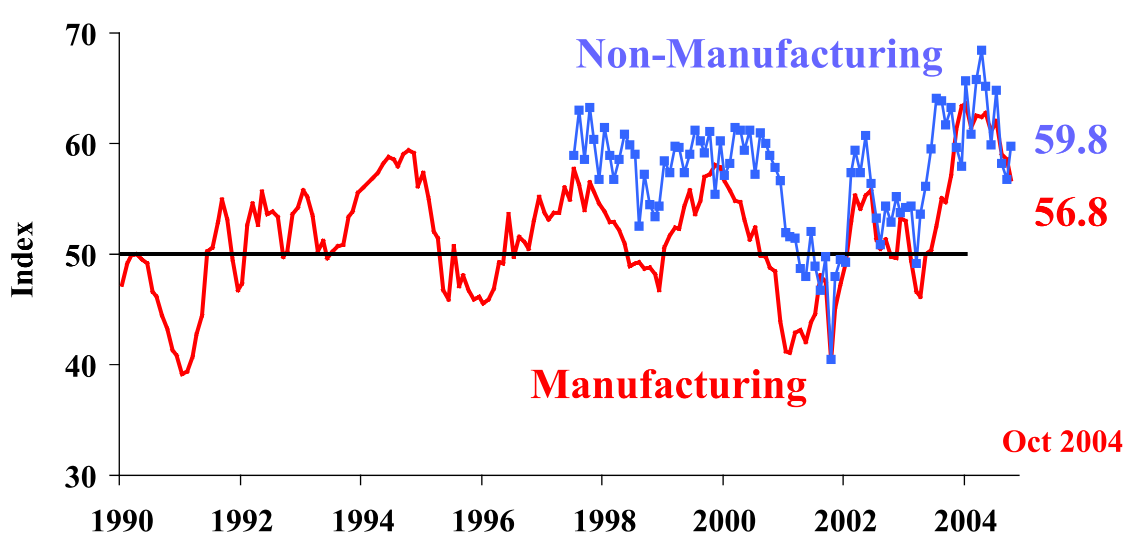


Source: U.S. Bureau of Labor Statistics

Major Economic Indicators

Major U.S. economic indicators point to continued, but likely slowing, economic growth. The Institute for Supply Management's (ISM) manufacturing index, while signaling continued growth, has declined the past three months. Similarly, the ISM non-manufacturing index, while rising in October, has remained below 60 for three straight months. A reading of 50 indicates a growing sector.

ISM Indices Signal Growth in Manufacturing and Services



Source: Institute for Supply Management.

For over a year, new durable goods orders have trended upward. However, in recent months, durable goods order growth has moderated, disappointing expectations. Using a three-month trailing average, new durable goods orders are 9.2 percent higher than a year ago. Capacity utilization remains near 20-year lows. After having trended upward earlier this year, capacity utilization growth has flattened out in recent months. Equipment investment has grown at faster than a 10 percent rate in five of the past six quarters.

While recent retail sales growth has been uneven, retail sales were up 7.6 percent from a year ago. Consumer sentiment fell over the late summer and early fall. Rising energy prices and disappointing jobs growth depressed the index in recent months. Consumer sentiment then rose slightly in November. The ABC News consumer comfort index, which measures consumers' attitude toward current economic conditions, has largely moved sideways since June 2004.

In October, the index of leading economic indicators fell for the fifth straight month.

Employment

Employment has now increased every month since September 2003. However, this growth has been uneven. Employment grew at a tepid rate through the end of 2003 before posting moderate growth the first half of 2004. Employment growth then slowed over the summer before reporting strong growth in October. Despite employment growth for over a year, U.S. employment remains half a million jobs below the March 2001 peak and some sectors are still struggling.

The manufacturing sector has been particularly hard hit. Even before the recession, the manufacturing sector was losing jobs. Beginning in August 2000, U.S. manufacturing employment fell for 42 straight months. Manufacturing employment then reported solid gains in early 2004. However, in recent months, manufacturing employment has declined. Over the past four years the manufacturing sector has lost nearly 3 million jobs. Rapid productivity gains allowed firms to reduce payroll employment even as they continued to increase output.

U.S. employment indicators are stronger and indicate that employment should continue to rise. Recent indicators also suggest that employers are laying off fewer workers and are beginning to hire additional workers.

Compared to a year ago, initial unemployment claims have fallen from around 380,000 to around 330,000 (four week moving average). Weekly initial unemployment claims have largely walked sideways since April 2004. At 332,000, the most recent four-week average of initial claims has returned to its pre-recession level.

The Institute for Supply Management's (ISM) manufacturing employment index component has shown expansion each month since late 2003. However, in the most recent month, the employment index fell to its lowest level since January 2004. The non-manufacturing ISM employment index has signaled expansion in 12 of the past 13 months. The Challenger Report count of announced layoffs fell sharply in early 2004 and then remained essentially flat through September 2004. Announced layoffs rose sharply in September before moderating somewhat in October.

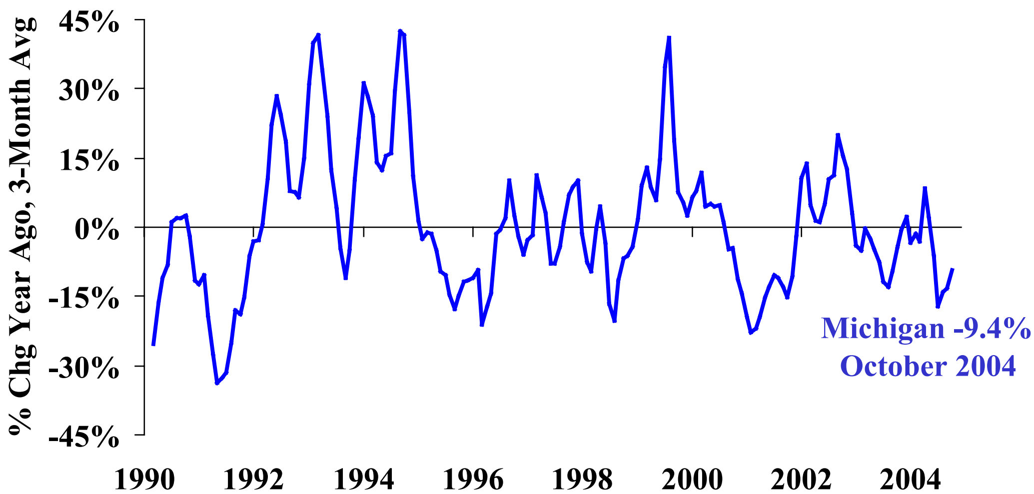
Weekly hours worked, a leading indicator for employment, have remained flat this year. The October 2004 reading showed average hours worked at 33.8 hours, unchanged from last month.

Vehicle Sales and Production

Rebates coupled with low financing rates have helped maintain vehicle sales above 16 million units. In 2003, light vehicle sales averaged 16.6 million units. Through October, year-to-date light vehicle sales have averaged 16.7 million units. Over the past few years, imports and transplants have continued to increase their market share. Thus, traditional Big Three market share has continued to fall, which is a concern for the Michigan economy.

Averaged over the past three months, U.S. vehicle production in October 2004 has decreased 3.7 percent while Michigan vehicle production is down 9.4 percent.

Michigan Vehicle Production Down from Year Ago



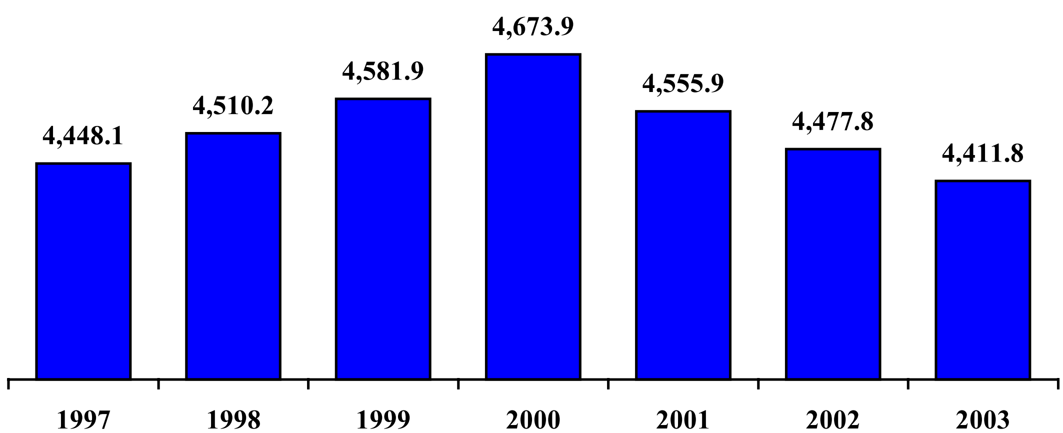
Source: Automotive News and Michigan Department of Treasury.

Current Michigan Economic Conditions

Employment

Michigan's economy relies heavily on the performance of the manufacturing sector in general and the auto industry specifically. Given extremely weak manufacturing employment performance, declining vehicle production, continued declines in Big 3 market share along with continued supply rationalization among vehicle suppliers, Michigan's employment performance has been below the national average. Substantial productivity gains in the vehicle industry have also contributed to Michigan's sub-par employment performance. Over the past three years, the annual average for wage and salary employment has fallen. Through October, state employment is down compared to a year ago. From Michigan's employment peak in June 2000 compared to October 2004, Michigan has lost 317,000 jobs. By this time after the 1990-1991 recession, Michigan employment had risen nearly 200,000 jobs *above* its pre-recession peak.

Michigan Wage and Salary Employment Declines Past Three Years
(annual average in thousands)



Source: Bureau of Labor Statistics.

Michigan manufacturing employment has declined even more sharply. Since June 2000, Michigan manufacturing employment has fallen by more than 200,000 jobs. Michigan has lost more than one out of every five manufacturing jobs it had at the state's employment peak.

Unemployment Rate

Michigan's annual average unemployment rate for 2003 was 7.3 percent, the highest level since 1992. The most recent monthly unemployment reading in October 2004 was 6.6 percent. The state's unemployment rate is down 1.0 percentage point from a year ago but substantially above its lows, around 3.0 percent, during the expansion of the late 1990s.

Personal Income

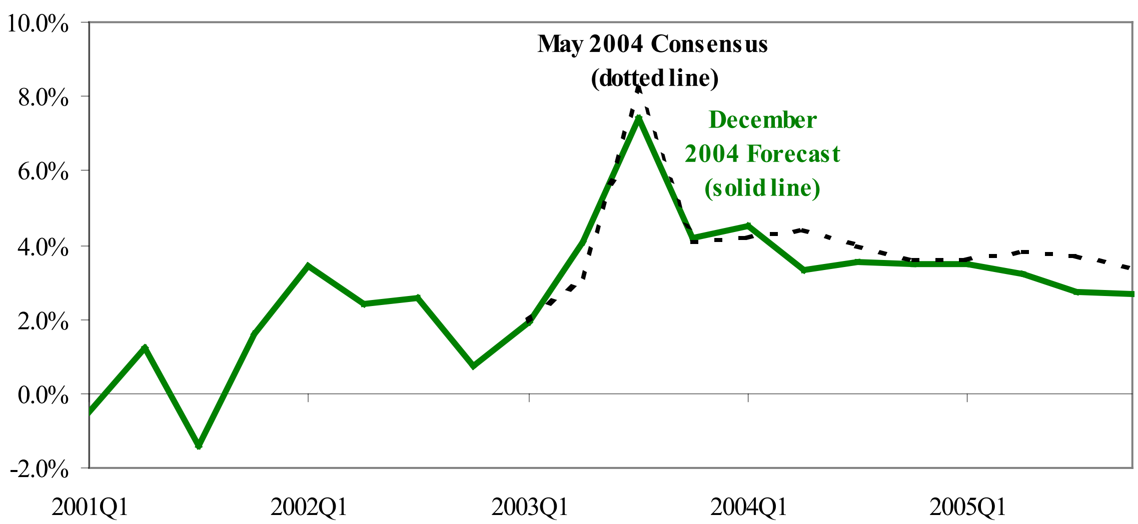
Michigan's personal income increased 4.1 percent in 2003; wages and salaries grew 1.8 percent. Wages and salaries grew 0.6 percent year-over-year in the second quarter of 2004. Overall personal income grew 3.1 percent year over year in the second quarter. (Large contributions to employee pension and health insurance plans largely account for the apparent incongruity between overall personal income growth and wage and salary growth).

2004 and 2005 U.S. Economic Outlook

Summary

Real GDP is forecast to grow 4.4 percent in 2004 and 3.3 percent in 2005. Real GDP grew 3.0 percent in 2003.

Real GDP Forecast Comparisons

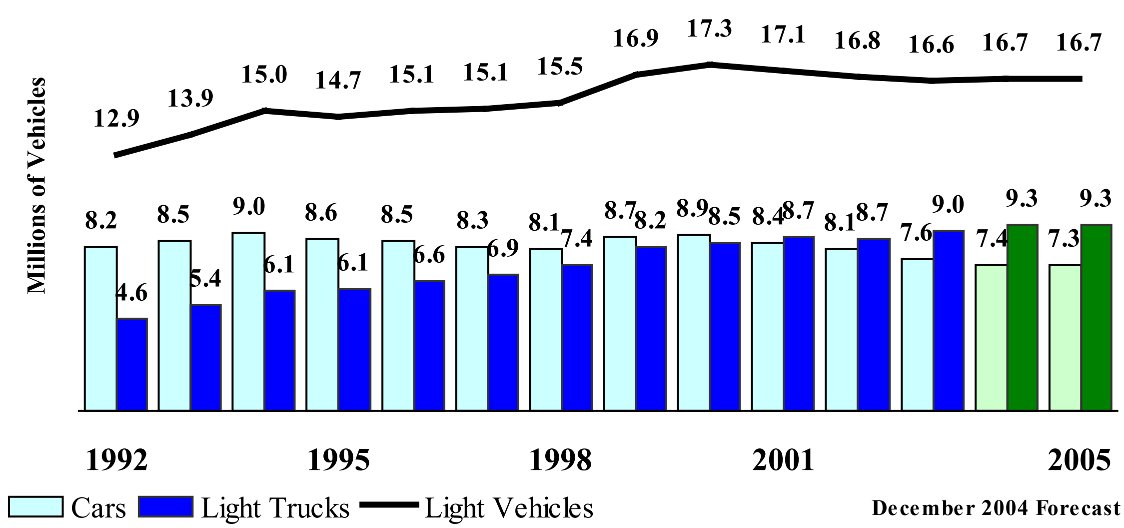


Business investment growth is forecast to increase in 2004 and remain steady in 2005. Investment growth is projected to rise 10.0 percent in 2004 and 9.9 percent in 2005, up from 3.3 percent in 2003. The expiration of bonus depreciation at the end of 2004 is expected to boost investment. Low capacity utilization rates will be offset by the need to replace increasingly obsolete machinery and by higher profits that will allow companies to make investments. Consumption is forecast to rise 3.6 percent in 2004 and 3.3 percent in 2005. A stronger labor market will help consumer spending and offset the impact of higher interest rates. Government spending growth is expected to slow in 2004 and 2005. Federal defense spending growth will remain strong in 2004 before slowing in 2005. State and local government spending will increase, albeit at a weak rate, as some individual state economies make stronger recoveries. Net exports are forecast to fall sharply in 2004 and decline again in 2005. Projected light vehicle sales are nearly unchanged from 2003 with projected sales of 16.7 million in both 2004 and 2005.

Inflation will remain moderate throughout the forecast horizon. As measured by the consumer price index (CPI), consumer prices are expected to rise 2.7 percent in both 2004 and 2005. Interest rates are forecast to remain low even as the Federal Reserve continues to tighten.

U.S. employment is forecast to rise in 2004 and 2005 with gains projected throughout the forecast horizon. Thus, the U.S. unemployment rate is expected to fall from 6.0 percent in 2003 to 5.5 percent in 2004 and 5.4 percent in 2005.

Motor Vehicle Sales Stable



Source: Bureau of Economic Analysis, U.S. Department of Commerce, and Administration Forecast, December 2004.

<u>Assumptions</u>

Oil prices are projected to stay around $50 a barrel through mid 2005 before beginning to decline slowly. The forecast assumes that $50 a barrel oil prices have a moderate impact on the economy.

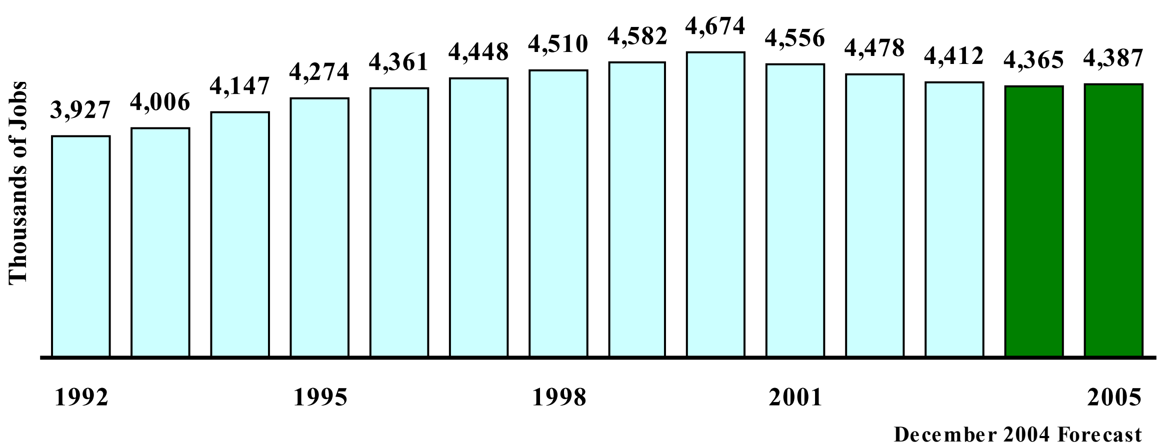
With stronger employment readings and commodity price pressures, the Federal Reserve is expected to continue to increase the federal funds rate at a moderate pace.

The household savings rate is forecast to stay around 1.0 percent throughout the forecast. Stock prices are expected to post modest gains over the forecast horizon.

2004 and 2005 Michigan Economic Outlook

Michigan employment is forecast to decline in 2004 for the fourth straight year with modest growth in 2005. Weak growth in manufacturing employment will constrain Michigan employment increases. After declining in the third quarter, Michigan wage and salary employment is forecast to grow by 6,000 jobs in the fourth quarter of 2004. In 2005, employment is forecast to increase an average of 10,000 jobs per quarter. Wage and salary employment is forecast to decline 1.1 percent in 2004. Wage and salary employment is projected to increase 0.5 percent in 2005. Michigan's unemployment rate is forecast to fall to 6.7 percent in 2004 before rising to 6.9 percent in 2005.

Michigan Wage and Salary Employment



Source: Michigan Department of Labor and Economic Growth, U.S. Bureau of Labor Statistics and Administration Forecast.

Wage and salary income is projected to rise 2.4 percent in 2004. In 2005, wage and salary income is projected to increase 4.3 percent as employment gains continue. Michigan personal income is forecast to rise 3.8 percent in 2004 and 5.4 percent in 2005.

Inflation, as measured by the Detroit CPI, is forecast to be 1.4 percent in 2004 and 2.1 percent in 2005. As a result, real Michigan personal income (inflation adjusted) is expected to rise 2.3 percent in 2004 and 3.2 percent in 2005.

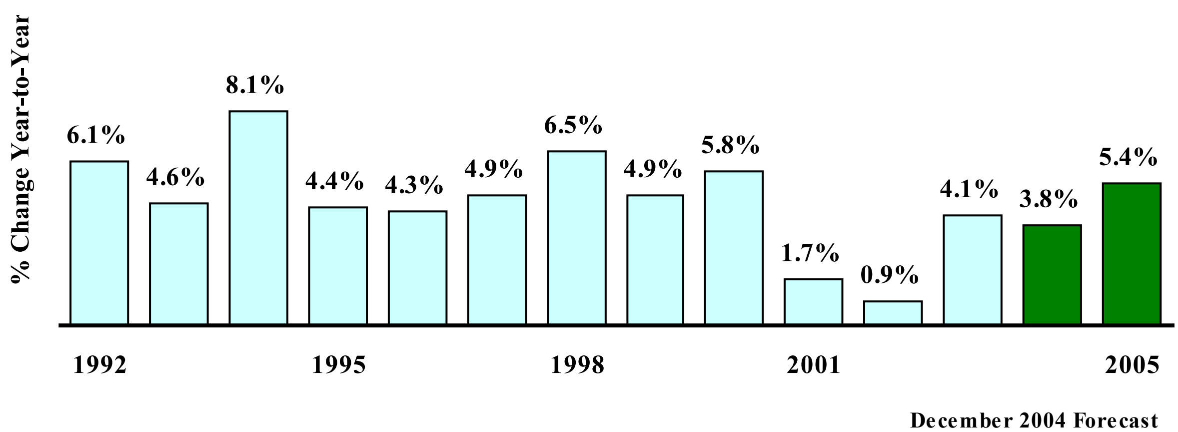
Table 1

Adminstration Economic Forecast

December 2004

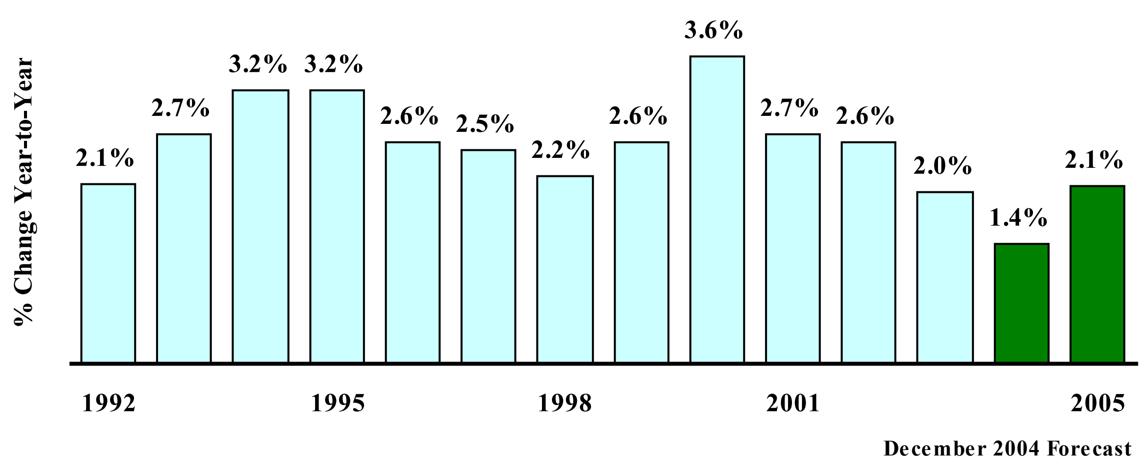
	Calendar 2002 Actual	Calendar 2003 Actual	Percent Change from Prior Year	Calendar 2004 Forecast	Percent Change from Prior Year	Calendar 2005 Forecast	Percent Change from Prior Year
United States							
Real Gross Domestic Product (Billions of Chained 2000 Dollars)	$10,075	$10,381	3.0%	$10,833	4.4%	$11,190	3.3%
Implicit Price Deflator GDP (2000 = 100)	104.1	106.0	1.8%	108.2	2.1%	110.6	2.2%
Consumer Price Index (1982-84 = 100)	179.9	184.0	2.3%	189.0	2.7%	194.1	2.7%
Personal Consumption Deflator (2000 = 100)	103.5	105.5	1.9%	107.8	2.2%	110.1	2.1%
3-month Treasury Bills Interest Rate (percent)	1.6	1.0		1.3		2.3	
Aaa Corporate Bonds Interest Rate (percent)	6.5	5.7		5.6		5.7	
Unemployment Rate - Civilian (percent)	5.8	6.0		5.5		5.4	
Light Vehicle Sales (millions of units)	16.8	16.6	-0.9%	16.7	0.4%	16.7	0.0%
Passenger Car Sales (millions of units)	8.1	7.6	-6.0%	7.4	-3.2%	7.3	-0.3%
Light Truck Sales (millions of units)	8.7	9.0	3.8%	9.3	3.4%	9.3	0.3%
Import Share of Light Vehicles (percent)	19.6	19.9		19.7		20.6	
Michigan							
Wage and Salary Employment (thousands)	4,478	4,412	-1.5%	4,365	-1.1%	4,387	0.5%
Unemployment Rate (percent)	6.2	7.3		6.7		6.9	
Personal Income (millions of dollars)	$302,019	$314,460	4.1%	$326,378	3.8%	$343,904	5.4%
Real Personal Income (millions of 1982-84 dollars)	$168,820	$172,307	2.1%	$176,325	2.3%	$181,960	3.2%
Wages and Salaries (millions of dollars)	$173,339	$176,493	1.8%	$180,785	2.4%	$188,564	4.3%
Detroit Consumer Price Index (1982-84 = 100)	178.9	182.5	2.0%	185.1	1.4%	189.0	2.1%
Detroit CPI Fiscal Year (1982-84 = 100)	177.5	182.0	2.5%	184.4	1.3%	188.3	2.1%

Michigan Personal Income Growth Stronger in 2005



Source: Bureau of Economic Analysis, U.S. Department of Commerce, and Administration Forecast, December 2004.

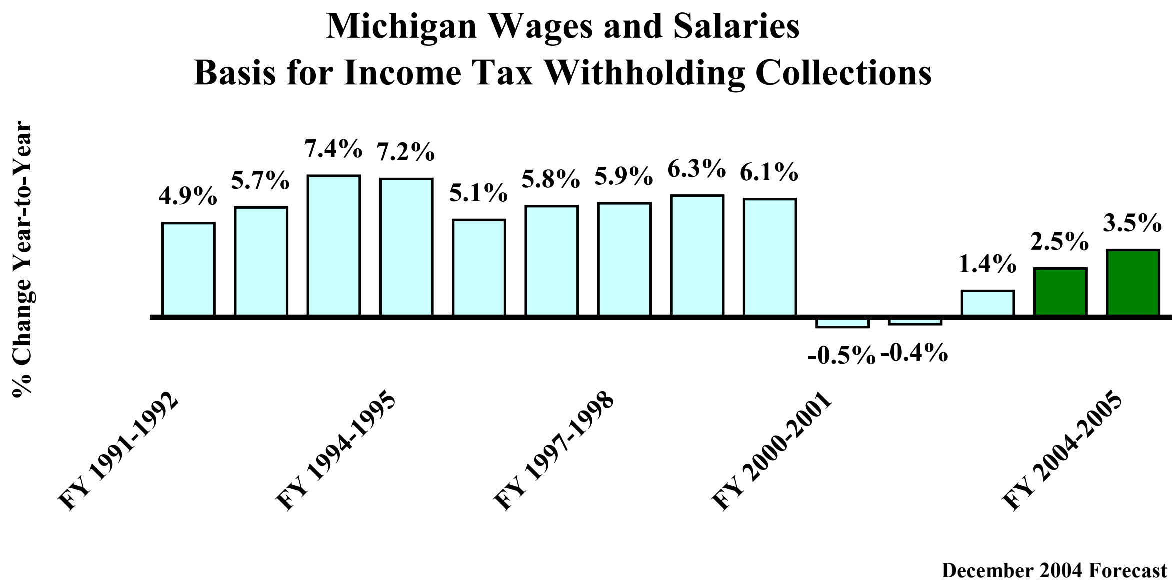
Inflation Rate Remains Low
Detroit CPI



Source: U.S. Bureau of Labor Statistics and Administration Forecast, December 2004.

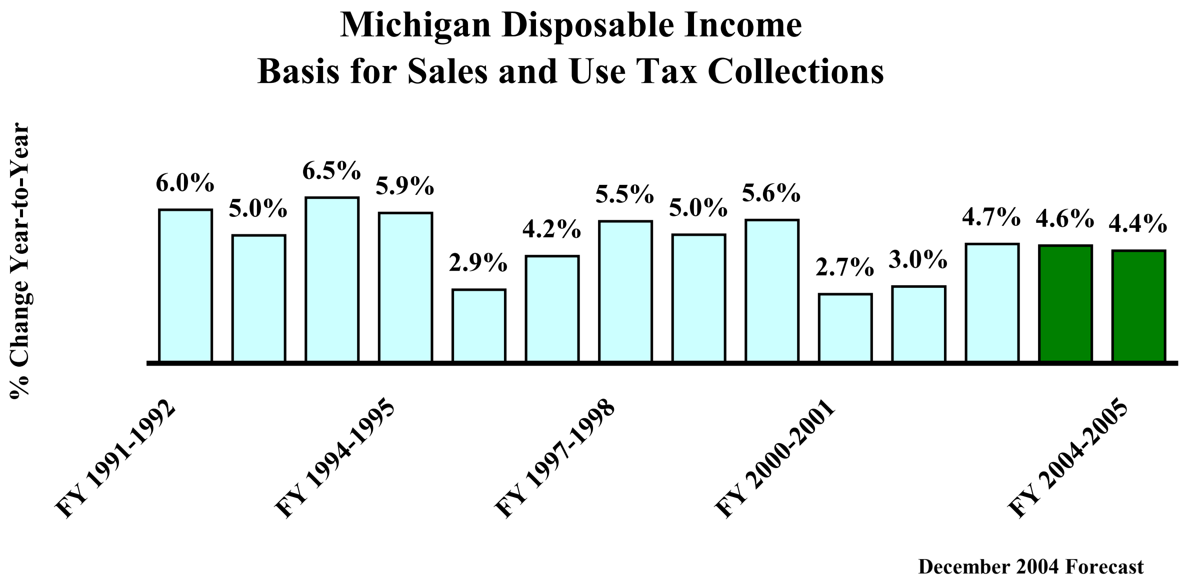
Fiscal Year Economics

Michigan's largest taxes are the individual income tax, which includes refunds, ($5.8 billion) and sales and use taxes ($7.7 billion). Income tax withholding is the largest income tax component. Withholding ($6.5 billion) is most affected by growth in wages and salaries. Michigan wages and salaries are expected to have grown 2.5 percent in FY 2004 and to grow 3.5 percent in FY 2005. The FY 2004 and FY 2005 forecasted increases follow three consecutive years of slight declines or slight growth, and are substantially slower than growth reported through much of the 1990s.



Source: Bureau of Economic Analysis, U.S. Department of Commerce, and Administration Forecast, December 2004.

Sales and use taxes depend primarily on Michigan disposable (after tax) income and inflation. Disposable income is expected to have risen 4.6 percent in FY 2004 and to increase 4.4 percent in FY 2005. Disposable income rises faster than wage and salary income because of federal income tax rate cuts. The inflation rate rose 1.3 percent in FY 2004 and is expected to increase 2.1 percent in FY 2005.



Source: Research Seminar in Quantitative Economics, University of Michigan, and Administration Forecast, December 2004.

Forecast Risks

U.S. employment has increased each month for over a year. However, employment at the national level is below the pre recession peak and Michigan employment is still well below the previous recession peaks. The baseline forecast predicts that sustained and stronger growth will spur U.S. employment increases in 2004 and modest Michigan employment gains beginning at the end of 2004. If the employment gains do not materialize, economic growth will decline as consumer and business spending retrenches. In large part, Michigan employment is still declining. If Michigan's employment level does not begin to increase soon, state economic growth will be below forecast levels.

If business investment is above projected levels, economic growth may be more than forecast. For the Michigan economy, Big Three market share is important. Sharp declines in market share would affect the Michigan economy adversely compared to other states. Similarly, faster (slower) productivity growth may increase (decrease) employment and overall economic growth. Faster (slower) inventory investment will increase (decrease) economic growth.

Continued higher oil and natural gas prices could curb growth. Weaker growth abroad could also slow domestic growth as exports decline. Equity prices are expected to rise modestly. Slower growth or outright declines could slow consumption and investment spending. If the U.S. dollar declines sharply, inflation risks would increase and financial markets may be roiled. Geopolitical concerns also pose a risk to the forecast.

ADMINISTRATION REVENUE ESTIMATES

December 3, 2004

Revenue Estimate Overview

The revenue estimates presented in this section consist of baseline revenues, revenue adjustments, and net revenues. Baseline revenues provide an estimate of the effects of the economy on tax revenues. For these estimates, FY 2003 is the base year. Estimates will be presented on an FY 2004 base starting in January of 2005. Any non-economic changes to the taxes occurring in FY 2004 and FY 2005 are not included in the baseline estimates. Non-economic changes are referred to in the tables as "tax adjustments." The net revenue estimates are the baseline revenues adjusted for tax adjustments.

This treatment of revenue is best illustrated with an example. Suppose tax revenues are $10.0 billion in a given year, and that based on the economic forecast, revenues are expected to grow by 5.0 percent per year. Baseline revenue would be $10.0 billion in Year 1, $10.5 billion in Year 2, and $11.0 billion in Year 3. Assume a rate cut is in place that would reduce revenues by $100 million in Year 1, $200 million in Year 2, and $300 million in Year 3. If Year 1 is the base year, the revenue adjustments for Year 1 would be $0 since the tax cut for this year is included in the base. The revenue adjustments for Year 2 would be $100 million, and the revenue adjustments for Year 3 would be $200 million, since the revenue adjustments are compared to the base year.

In the example above, the baseline revenues would be $10.0 billion, $10.5 billion, and $11.0 billion, for Years 1 through 3, respectively. The revenue adjustments would be $0 in Year 1, $100 million in Year 2, and $200 million in Year 3. The $200 million in Year 3 represents the tax cuts since Year 1. Net revenue would be $10.0 billion in Year 1, $10.4 billion in Year 2, and $10.8 billion in Year 3.

The revenue figures presented below are on a Consensus basis. Generally speaking, the Consensus estimates do not include certain one-time budget measures, such as withdrawals from the Budget Stabilization Fund, the sale of buildings, etc. The figures also assume the full statutory amount for revenue sharing payments. In addition, the estimates only include enacted legislation and do not include the effects of any proposed changes. The School Aid Fund estimates consist of taxes plus the transfer from the State Lottery Fund.

FY 2004 Revenue Outlook

FY 2004 GF-GP revenue is expected to be $7,968.1 million, a 1.2 percent GF-GP baseline increase and a 0.1 percent increase after tax adjustments. The FY 2004 GF-GP revenue estimate is $2.3 million below the Adjusted May Consensus estimate. The Adjusted May Consensus estimates are the May Consensus estimates adjusted to include revenue items enacted after the May Consensus Conference. For example, the tobacco tax was increased in July of 2004, after the May Conference, and the effects of this increase are incorporated into the adjusted May estimates. The May estimates were adjusted for changes enacted after the Conference so that they can be directly compared with the December estimates. SAF revenue is forecast to be $10,551.9 million, a 1.7 percent SAF baseline increase, and a 1.5 percent decline after tax adjustments (See Table 2). The FY 2004 SAF revenue estimate is $7.4 million below the Adjusted May Consensus estimate.

Table 2

FY 2003-04 Administration Revenue Estimates

(millions)

	Adjusted Consensus May 18, 2004		Preliminary December 3, 2004		
	Amount	**Growth**	**Amount**	**Growth**	**Change**
General Fund - General Purpose					
Baseline Revenue	$8,076.0	1.7%	$8,037.0	1.2%	
Tax Cut Adjustments	($105.6)		($68.9)	NA	
Net Resources	$7,970.4	0.1%	$7,968.1	0.1%	($2.3)
School Aid Fund					
Baseline Revenue	$10,446.3	1.5%	$10,434.5	1.7%	
Tax Cut Adjustments	$113.0		$117.3	NA	
Net Resources	$10,559.3	-1.5%	$10,551.9	-1.5%	($7.4)
Combined					
Baseline Revenue	$18,522.3		$18,471.6	1.5%	
Tax Cut Adjustments	$7.4		$48.4	NA	
Net Resources	$18,529.7	-0.8%	$18,520.0	-0.8%	($9.7)

Prepared By: Economic and Revenue Forecasting Division, Michigan Department of Treasury

FY 2005 Revenue Outlook

Baseline revenue growth improves in FY 2005 with the improving economy. FY 2005 GF-GP revenue is expected to be $7,899.0 million, a 2.8 percent baseline increase and a 0.9 percent reduction after tax adjustments. Net GF-GP growth is slowed by a number of factors including the income tax rate cut, the continued phase-out of the state's estate tax, and the shift of some tobacco revenues to the Medicaid Trust Fund. The FY 2005 estimate is $196.4 million below the Adjusted May Consensus estimate. The large decline is due to the economic forecast calling for a weaker recovery than was forecast in May. SAF revenue is forecast to be $10,944.0 million, representing 3.7 percent SAF baseline growth and 3.7 percent growth after tax adjustments. The FY 2005 SAF estimate is $52.7 million below the Adjusted May Consensus estimate (See Table 3).

Table 3

FY 2004-05 Administration Revenue Estimates

(millions)

	Adjusted Consensus May 18, 2004		Administration December 3, 2004		
	Amount	**Growth**	**Amount**	**Growth**	**Change**
General Fund - General Purpose					
Baseline Revenue	$8,417.2	4.2%	$8,268.3	2.9%	
Tax Cut Adjustments	($321.8)		($369.3)	NA	
Net Resources	$8,095.4	1.6%	$7,899.0	-0.9%	($196.4)
School Aid Fund					
Baseline Revenue	$10,874.2	4.1%	$10,819.1	3.7%	
Tax Cut Adjustments	$122.5		$124.9	NA	
Net Resources	$10,996.7	4.1%	$10,944.0	3.7%	($52.7)
Combined					
Baseline Revenue	$19,291.4	4.2%	$19,087.4	3.3%	
Tax Cut Adjustments	($199.3)		($244.3)	NA	
Net Resources	$19,092.1	3.0%	$18,843.0	1.7%	($249.1)

Prepared By: Economic and Revenue Forecasting Division, Michigan Department of Treasury

Constitutional Revenue Limit

Article IX, Section 26, of the Michigan Constitution establishes a limit on the amount of revenue state government can collect in any given fiscal year. The revenue limit for a given fiscal year is equal to 9.49 percent of the state's personal income for the calendar year prior to the year in which the fiscal year begins. FY 2002 revenue is compared to CY 2000 personal income. If revenues exceed the limit by less than 1 percent, the state may deposit the excess into the Budget Stabilization Fund (BSF). If the revenues exceed the limit by more than 1 percent, the excess revenue is refunded to taxpayers via the income and single business taxes.

FY 2003 revenues were $4.2 billion below the revenue limit. State revenues will be well below the limit for FY 2004 and FY 2005 due to the effects of tax cuts and the economic slowdown on the state's revenue stream. FY 2004 revenues are expected to be $4.9 billion below the limit, and FY 2005 revenues are expected to be $5.6 billion below the limit (See Table 4).

Table 4

Administration Constitutional Revenue Limit Calculation

(millions)

	FY 2002 Actual Mar 2003	FY 2003 Actual Mar 2004	FY 2004 Admin May 2004	FY 2005 Admin May 2004
Revenue Subject to Limit	$23,546.0	$24,061.6	$23,950.5	$24,262.7
Revenue Limit	**CY 2000**	**CY 2001**	**CY 2002**	**CY 2003**
Personal Income	$289,390	$297,609	$303,745	$314,460
Ratio	9.49%	9.49%	9.49%	9.49%
Revenue Limit	$27,463.1	$28,243.1	$28,825.4	$29,842.2
Amount Under (Over) Limit	**$3,917.1**	**$4,181.5**	**$4,874.9**	**$5,579.5**

Budget Stabilization Fund Calculation

The Management and Budget Act contains provisions for calculating a recommended deposit or withdrawal from the BSF. The calculation looks at personal income net of transfer payments adjusted for inflation. The change in this figure for the calendar year determines whether a pay-in or pay-out is dictated. If the formula calls for a deposit into the BSF, the deposit is made in the next fiscal year. If the formula calls for a withdrawal, the withdrawal is made during the current fiscal year.

If real personal income grows by more than 2 percent in a given calendar year, the fraction of income growth over 2 percent is multiplied by the current fiscal year's GF-GP revenue to determine the pay-in for the next fiscal year. If real personal income declines, the percentage deficiency under zero is multiplied by the current fiscal year's GF-GP revenue to determine the withdrawal available for the current fiscal year. If the change in real personal income is between 0 and 2 percent, no pay-in or withdrawal is indicated.

Real calendar year personal income for Michigan is expected to increase by 2.3 percent in 2004. Therefore, a pay-in of $23.9 million is called for in FY 2005 (See Table 5).

Table 5

Budget and Economic Stabilization Fund Calculation Based on CY 2004 Personal Income Growth Administration Calculation

	CY 2003	CY 2004
Michigan Personal Income	$ 314,460 [1]	$ 326,378 [2]
less Transfer Payments	$ 46,874 [1]	$ 49,049 [2]
Income Net of Transfers	$ 267,586	$ 277,329
Detroit CPI	1.814 [3]	1.837 [3]
for 12 months ending	(June 2003)	(June 2004)
Real Adjusted Michigan Personal Income	$ 147,512	$ 150,968
Change in Real Adjusted Personal Income		2.3%
Excess over 2%		0.3%
GF-GP Revenue Fiscal Year 2003-2004		$ 7,968.1

	FY 2004-2005
BSF Pay-In Calculated for FY 2005	$ 23.9

Notes:

(1) Personal Income and Transfer Payments, Bureau of Economic Analysis, October 2004.

(2) Personal Income and Transfer Payments, Admin Forecast, December 2004.

(3) Detroit Consumer Price Index, Average of 6 monthly values reported by BLS for each 12-month period.

School Aid Fund Revenue Adjustment Factor

The School Aid Fund (SAF) revenue adjustment factor for the next fiscal year is calculated by dividing the sum of current year and subsequent year SAF revenue by the sum of current year and prior year SAF revenue. For example, the FY 2005 SAF revenue adjustment factor is calculated by dividing the sum of FY 2004 and FY 2005 SAF revenue by the sum of FY 2003 and FY 2004 SAF revenue. The SAF revenue totals are adjusted for any change in the rate and base of the SAF taxes. The year for which the adjustment factor is being calculated is used as the base year for any tax adjustments. For FY 2005, the SAF revenue adjustment factor is calculated to be 1.0269 (See Table 6).

Table 6

Administration School Aid Revenue Adjustment Factor

For Fiscal Year FY 2005

	FY 2002-03	FY 2003-04	FY 2004-05
Baseline SAF Revenue	$10,255.7	$10,434.5	$10,819.1
Balance Sheet Adjustments	$459.2	$117.3	$124.9
Net SAF Estimates	$10,714.8	$10,551.9	$10,944.0
Adjustments to FY 2005 Base Year	($334.2)	$23.0	$0.0
Baseline Revenue on a FY 2005 Base	$10,380.6	$10,574.9	$10,944.0

School Aid Fund Revenue Adjustment Calculation for FY 2004-05

Sum of FY 2002-03 & FY 2003-04	$10,380.6	+	$10,574.9	=	$20,955.5
Sum of FY 2003-04 & FY 2004-05	$10,574.9	+	$10,944.0	=	$21,518.9

FY 2004-05 Revenue Adjustment Factor	**1.0269**

Revenue Detail

The estimated tax and revenue totals include the effects of all enacted tax changes except sales tax savings resulting from reductions in revenue sharing payments to local units. The revenue totals by tax are presented separately for GF-GP and for the SAF (See Tables 7 and 8). Tax totals for the income, sales, use, and tobacco taxes for all funds are also included (See Table 9).

Table 7

Administration General Fund General Purpose Revenue Detail

(millions)

	FY 2003		FY 2004		FY 2005	
	Amount	**Growth**	**Amount**	**Growth**	**Amount**	**Growth**
GF-GP Tax Amounts						
Income Tax	$3,960.9	-6.4%	$3,959.3	0.0%	$3,966.6	0.2%
Sales	$63.7	-27.6%	$103.0	61.6%	$122.6	19.0%
Use	$819.6	-5.6%	$878.4	7.2%	$913.2	4.0%
Cigarette	$289.2	48.4%	$241.8	-16.4%	$122.8	-49.2%
Beer & Wine	$51.1	2.2%	$51.5	0.8%	$52.0	1.0%
Liquor Specific	$31.1	4.0%	$33.0	6.1%	$32.6	-1.2%
Single Business Tax	$1,842.9	-7.1%	$1,786.3	-3.1%	$1,846.1	3.3%
Insurance Co. Premium	$231.1	1.8%	$221.0	-4.4%	$231.0	4.5%
Telephone & Telegraph	$124.2	-9.5%	$101.3	-18.4%	$95.3	-5.9%
Inheritance Estate	$98.6	-24.7%	$76.0	-22.9%	$39.0	-48.7%
Intangibles	($1.4)	0.0%	$0.1	0.0%	$0.0	0.0%
Casino Wagering	$0.0	0.0%	$3.2	NA	$42.9	NA
Horse Racing	$0.0	0.0%	$2.0	0.0%	$0.0	0.0%
Oil & Gas Severance	$47.9	56.0%	$54.4	13.6%	$47.4	-12.9%
GF-GP Other Taxes	$52.6	-57.4%	$24.5	-53.4%	$35.8	46.1%
Total GF-GP Taxes	$7,611.4	-6.0%	$7,535.8	-1.0%	$7,547.2	0.2%
GF-GP Non-Tax Revenue						
Federal Aid	$47.2	91.1%	$66.1	40.0%	$30.0	-54.6%
From Local Agencies	$0.9	12.5%	$2.9	222.2%	$2.5	-13.8%
From Services	$8.5	63.5%	$17.8	109.4%	$18.0	1.1%
From Licenses & Permits	$16.9	2.4%	$55.2	226.6%	$54.0	-2.2%
Miscellaneous	$100.0	-24.0%	$72.0	-28.0%	$125.6	74.4%
Short Term Note Int.	($8.0)	0.0%	$0.0	0.0%	$0.0	0.0%
Interfund Interest	($13.3)	11.8%	($22.2)	66.9%	($75.0)	237.8%
Liquor Purchase	$126.8	7.3%	$139.4	9.9%	$133.0	-4.6%
Charitable Games	$11.2	-7.4%	$12.2	8.9%	$11.0	-9.8%
Transfer From Escheats	$57.3	79.6%	$88.9	55.1%	$52.8	-40.6%
Other Non Tax	$0.0	0.0%	$0.0	0.0%	$0.0	0.0%
Total Non Tax	$347.5	5.6%	$432.3	24.4%	$351.9	-18.6%
Total GF-GP Revenue	$7,958.9	-5.6%	$7,968.1	0.1%	$7,899.0	-0.9%

Table 8

Administration School Aid Fund Revenue Detail

	FY 2003		FY 2004		FY 2005	
	Amount	Growth	Amount	Growth	Amount	Growth
School Aid Fund						
Income Tax	$1,847.8	-0.7%	$1,893.6	2.5%	$1,972.6	4.2%
Sales Tax	$4,681.4	-0.3%	$4,719.0	0.8%	$4,916.6	4.2%
Use Tax	$410.2	-5.8%	$439.6	7.2%	$456.5	3.9%
Liquor Excise Tax	$30.6	5.2%	$32.4	5.9%	$32.6	0.6%
Cigarette	$471.4	22.1%	$465.5	-1.3%	$463.9	-0.3%
Other Tobacco	$17.7	1.0%	$16.0	-9.7%	$16.0	0.0%
State Ed Prop Tax	$2,127.5	34.3%	$1,765.2	-17.0%	$1,864.3	5.6%
Real Estate Transfer	$275.5	8.9%	$314.1	14.0%	$306.4	-2.5%
Ind and Comm Facilities	$161.2	5.8%	$149.5	-7.3%	$145.5	-2.7%
Casino (45% of 18%)	$90.9	0.0%	$96.2	5.8%	$96.3	0.1%
Commercial Forest	$2.8	12.0%	$2.7	-3.6%	$2.8	3.7%
Other Spec Taxes	$11.8	-7.8%	$13.3	12.7%	$12.0	-9.8%
Subtotal Taxes	$10,128.8	6.4%	$9,907.0	-2.2%	$10,285.5	3.8%
Lottery Transfer	$586.0	-4.5%	$644.9	10.1%	$658.5	2.1%
Total SAF Revenue	$10,714.8	5.7%	$10,551.9	-1.5%	$10,944.0	3.7%

Table 9

Administration Major Tax Totals

Major Tax Totals (Includes all Funds)						
Income Tax	$5,810.6	-4.7%	$5,854.5	0.8%	$5,940.7	1.5%
Sales Tax	$6,422.6	-0.2%	$6,476.6	0.8%	$6,747.2	4.2%
Use Tax	$1,229.8	-5.9%	$1,318.0	7.2%	$1,369.7	3.9%
Cigarette and Tobacco	$890.9	37.5%	$988.0	10.9%	$1,188.8	20.3%